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Internal Revenue Service

Department of the Treasury

Washington, D.C. 20224

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Person to Contact:

Telephone Number:

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Date:
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LEGEND:

Association =

State X =

Year 1 =

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Dear :

This is in response to a June 8, 1999, letter and subsequent correspondence submitted on behalf of Association requesting a ruling that the income of Association is excludible from gross income for federal income tax purposes under section 115(1) of the Internal Revenue Code. Association also has requested a ruling concerning its filing requirements. Pursuant to section 8.02(1) of Rev. Proc. 99-1, 1999-1 I.R.B. 6, 30, that ruling will be addressed in a separate response.

FACTS

Association, a State X corporation, was founded in Year 1 as a nonpartisan association of county governments in State X. Association's Articles of Incorporation (Articles) state that Association was created as a league of State X county governments to aid and assist State X counties in carrying out their public purposes and functions. The functions performed by Association allow State X counties to receive the benefits of improved service and reduced costs through cooperative efforts.

Association is governed by its Bylaws. Association's operations are conducted by a Board of Directors. The Board

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is composed of one member from each of State X's a senate districts, elected by commissioners of the counties contained within each senate district. County commissioners are the only persons eligible to serve as directors or officers of Association. The Executive Director of Association, a salaried employee, is an ex-officio, nonvoting member of the Board.

Association has proposed amendments to its Articles and Bylaws limiting membership in Association to counties in State X. Member counties pay dues determined on the basis of county population. Voting is also apportioned on the basis of population, with each commissioner's vote weighted according to the size of the population of the member county.

Association's Bylaws permit other associations or organizations that have similar purposes or objectives to those of Association to affiliate with Association. Association has proposed an amendment to its Bylaws limiting affiliation with Association to entities that are an integral part of State X, or a political subdivision of State X, or whose income is excludible under § 115(1) of the Code.

Association has proposed an amendment to its Articles providing that upon the dissolution of Association, all of its assets remaining after payment of its debts and obligations and the costs and expenses of such dissolution, will be distributed to State X county governments that are members in good standing of Association on the date of distribution.

LAW AND ANALYSIS

Section 115(1) of the Code provides that gross income does not include income derived from any public utility or the exercise of any essential governmental function and accruing to a state or political subdivision of a state.

When determining if § 115(1) applies, the Service considers all the facts and circumstances relating to the organization to determine whether the organization performs an essential governmental function and whether the income of the organization accrues to a state or a political subdivision of the state.

Rev. Rul. 90-74, 1990-2 C.B. 34, concerns an organization formed, operated, and funded by political subdivisions to pool their casualty risks and other risks

arising from their obligations concerning public liability, workers' compensation, or employees' health. The revenue ruling states that the income of such an organization is excluded from gross income under § 115(1) so long as private interests do not participate in the organization or benefit more than incidentally from the organization. The benefit to the employees of the insurance coverage obtained by the member political subdivisions was deemed incidental to the public benefit.

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that income from a fund, established under a written declaration of trust by a state, for the temporary investment of positive cash balances of a state and its political subdivisions, is excludable from gross income under § 115(1) of the Code. The ruling reasons that the investment of positive cash balances by a state or political subdivision in order to receive some yield on the funds until needed to meet expenses is a necessary incident of the power of the state or political subdivision to collect taxes and raise revenue.

Association was created to further the legitimate governmental and public functions of State X counties. Based upon Rev. Rul. 90-74 and Rev. Rul. 77-261, Association performs an essential governmental function within the meaning of § 115(1) of the Code.

In addition to the performance of an essential governmental function, for Association to qualify to exclude its income from gross income under § 115(1) of the Code, income of Association must accrue to State X or a political subdivision of State X.

Only counties in State X can be members of Association. No part of the net earnings of Association inures to the benefit of, or is distributable to, any private entity or individual. Upon dissolution of Association, all of its net assets will be distributed to State X counties, which are political subdivisions of State X. Thus, the income of Association accrues to political subdivisions of a state. Accordingly, the income of Association is excludible from gross income under § 115(1) of the Code.

HOLDING

Based on the information and representations submitted by Association, and provided that Association adopts in final form the proposed amendments to its Articles and Bylaws as described above, we hold that the income of

Association is excludible from gross income for federal income tax purposes under § 115(1) of the Code.

Except as specifically ruled upon above, no opinion is expressed or implied as to the federal tax consequences of the transaction described above under any other provision of the Internal Revenue Code. In particular, no opinion is expressed whether an annual return must be filed if Association has unrelated business taxable income under section 511 of the Code.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited as precedent.

In accordance with the provisions of a Power of Attorney currently on file, we are sending a copy of this ruling letter to your authorized representative.

Sincerely yours,

Assistant Chief Counsel
(Financial Institutions
and Products)

By: Alice M. Bennett
Alice M. Bennett
Chief, Branch 3

Enclosures:
Copy of this letter
Copy for section 6110 purposes

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